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No. 1281

IN THE

Supreme Court of the United States

OCTOBER TERM, 1966

PUBLIC SERVICE ELECTRIC AND GAS COMPANY,
Petitioner,

v.

FEDERAL POWER COMMISSION, TRANSCONTINENTAL GAS PIPE LINE CORPORATION AND TEXACO INC.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF IN OPPOSITION FOR RESPONDENT TEXACO INC.

OPINIONS BELOW

The opinion of the Court of Appeals issued January 18, 1967 is reported at 371 F. 2d 1 and is reprinted as Appendix A to the petition filed by Public Service Electric and Gas Company (Public Service) in No. 1281. The opinion and order of the Federal Power Commission (Commission) is reported at 33 F.P.C. 237 (1965). The opinion and order of the Commission on petition for rehearing is reported at 33 F.P.C. 818 (1965).

JURISDICTION

The jurisdictional requisites are adequately set forth in the petition.

QUESTIONS PRESENTED

1. Is a conventional transportation for hire arrangement by a natural gas pipeline converted into a series of sales merely because intermingling of the transportation gas with other gas transported and sold by the pipeline makes delivery to the shipper of the identical gas molecules previously tendered for transportation only coincidental?

2. Does the Natural Gas Act require an application for a certificate of public convenience and necessity for the operation of a 4½ mile existing intrastate refinery lead-in line utilized to deliver gas solely for own-use consumption where such line is currently subject to regulation by state authorities?

3. After considering an adequate record supporting all the elements of the public interest, and the public convenience and necessity, as they pertain to the proposed operations, was the Federal Power Commission justified in authorizing the transportation service?

STATUTES INVOLVED

The pertinent provisions of the Natural Gas Act (52 Stat. 821-833, as amended, 15 U.S.C. §§ 717-717w) are set forth in the Petition.

STATEMENT OF THE CASE

Transcontinental Gas Pipe Line Corporation (Transco) proposes to transport natural gas for Texaco Inc. (Texaco) from origins in the Texas-Louisiana Gulf Coast producing area to Texaco's Eagle Point Refinery near Westville, New Jersey. Texaco owns and produces the transport gas in the

Texas-Louisiana area and proposes to utilize it to convert certain refinery operations, now using fuel oil, to the use of its own natural gas in order to lower operating costs.

Transco is an interstate pipeline, and a natural gas company within the meaning of the Natural Gas Act,[1] and in that status, applied to the Federal Power Commission for authority to construct and operate the necessary additional facilities and to perform the transportation service. No party to this proceeding, or the hearings before the Federal Power Commission, opposes the proposed conversion of the refinery operations to the use of natural gas.

Texaco's refinery is located within the distribution territory of Public Service. Over many years prior to the negotiation of the Transco-Texaco transportation contract, Public Service sought ways and means to convert the Texaco refinery operations from fuel oil to natural gas, but was unable to offer a price which was low enough to economically justify conversion. At the hearing below, Public Service opposed the transportation service on numerous and often inconsistent grounds. It claimed, *inter alia,* that the service was improperly priced; that it would usurp capacity in the Transco line which should be held for future use; that Transco lacked the ability to deliver the proposed interruptible volumes because of inadequate "valley" capacity; and that Texaco would not receive significant benefits from the changeover.

The Commission had the benefit of an exhaustively detailed Examiner's Initial Decision which considered and rejected each of the Petitioner's contentions and recommended that a certificate of public convenience and necessity be issued to Transco to perform the transportation service. The Commission affirmed the Examiner's findings

[1] 52 Stat. 821 (1938), 15 U.S.C. §§ 717a, *et seq.*

in every regard, including findings that the proposed service would earn a generous return on the Transco facilities required, and that the revenues from such service would exceed the associated incremental costs by about $600,000 annually as a contribution to the support of Transco's other jurisdictional services. A denial of Transco's certificate application would result in the continued burning of fuel oil at the refinery and a loss of the above benefits to Transco's jurisdictional customers since the record conclusively establishes Public Service is unable to provide an economical alternative gas supply.

While the matter was pending below, the Commission on its own motion raised the question whether the transportation arrangement between Texaco and Transco as a result of commingling in the pipeline of the transport gas with Transco's wholesale gas supply " . . . involves a sale of gas by Texaco to Transco for resale by the latter so that the producer [Texaco] should be required to secure a certificate." (J.A. 1951-52) This legal issue had not been raised previously in the proceeding, but Public Service immediately embraced it as an additional basis on which to attack the transportation service. Petitioner contended that molecular commingling required that a traditional transportation contract should be tortured into a series of sales, and that Texaco should be required to obtain a certificate before tendering its gas to Transco for transport.

A unanimous Commission disagreed. The Supreme Court had decided *California* v. *Lo-Vaca Gathering Co.*, 379 U.S. 366 (1965), *before* the decision below was issued. The Commission considered Petitioner's contentions in the light of the *Lo-Vaca* decision and concluded that the instant transportation arrangement was not contrived to avoid federal regulation. It further found there was no reason or justification to depart from firmly established principles

of bailment relating to the commingling of fungible commodities in order to reform the transportation arrangement into a series of sales. The Commission also concluded that if it were to adopt Public Service's contentions, it would then lack authority to regulate the rate for the sale by Transco to Texaco at the delivery point to the refinery. This lack of jurisdiction, under the provisions of Sections 1(b) and 4 of the Natural Gas Act, would deny the financial benefits of the transportation service to the jurisdictional customers of Transco and one of the substantial public interest justifications for the instant proposal would be frustrated.

The United States Court of Appeals for the Third Circuit unanimously affirmed the decision of the Commission in all respects.

REASONS THE WRIT SHOULD BE DENIED

A. The Commingling Doctrine Does Not Convert a Jurisdictional Transportation Arrangement Into a Sale for Resale

The transportation arrangement between Texaco and Transco which is the subject of this litigation has been at all times fully subject to the jurisdiction of the Commission. After a comprehensive review of all public interest factors, it was certificated by the Commission under Section 7(c) of the Natural Gas Act as being within the public convenience and necessity. Accordingly, this case does not present any "regulatory gap" issues of the type raised in prior proceedings where parties sought to avoid Commission jurisdiction by resort to contract allocation of commingled sales volumes to non-jurisdictional markets or the direct assignment of leasehold interest to the pipeline purchaser (in-place sales). *California* v. *Lo-Vaca Gathering*

Co., 379 U.S. 366 (1965); *F.P.C.* v. *Amerada Petroleum Corp.*, 379 U.S. 687 (1965); *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965). In its Opinion, the Commission correctly noted:

> "The Commission has full and complete authority over the transportation agreement, and Texaco could not inject one Mcf of gas into Transco's interstate pipeline unless the Commission is satisfied that the transportation service is required by the public interest." (J.A. 2037)

The jurisdiction of the Commission conferred by Section 1(b) of the Natural Gas Act falls within three distinct categories: (1) the transportation of natural gas in interstate commerce; (2) its sale in interstate commerce for resale; and (3) natural gas companies engaged in such transportation or sale. *United Gas Pipe Line Co.* v. *F.P.C.*, ... U.S. ....., 17 L ed 2d 181, 185, 87 S Ct ..... (1966); *Panhandle Eastern Pipe Line Co.* v. *Public Service Commission of Indiana*, 332 U.S. 507, 516 (1947); *F.P.C.* v. *East Ohio Gas Co.*, 338 U.S. 464, 468 (1950). The statutory standard of public convenience and necessity established by Section 7 of the Natural Gas Act applies to each of the above jurisdictional activities.

Petitioner seeks to have this Court declare that the *Lo-Vaca* doctrine removes the concept of transportation for hire from the Natural Gas Act where commingling occurs simply because natural gas pipeline companies do not guarantee delivery to the shipper of the identical gas molecules which were previously tendered for transportation. Both the Commission and the court below correctly recognized that mere physical commingling does not compel rejection of historic notions of bailment relating to fungible commodities and require the transformation of a transportation agreement into a succession of sales. This

Court in both *Lo-Vaca* (379 U.S. at 370) and *Amerada* (379 U.S. at 691) indicated that there may be instances where original commingling does not require a particular transaction to be subject to the Commission's sale for resale jurisdiction. Therefore, the holdings of the Commission and the court below are in no way in conflict with this Court's decisions in *Lo-Vaca* and *Amerada*.

There is no justification for requiring the Commission to apply the molecular commingling doctrine to torture what obviously is intended to be a transportation arrangement into a series of sales. The Commission's scrutiny and control over the transportation service could have been no more complete had it reformed the transaction into a series of sales and certificated it under its sale for resale jurisdiction. The evidence adduced at the hearing below in support of Transco's transportation certificate application fully covered all factors which the Commission would look to if it were to require Texaco to apply for a second duplicative sales certificate covering the same transaction.[2]

Moreover, by being able to treat the Transco-Texaco agreement as "transportation" rather than a "sale for resale," the Commission was able to avoid certain undesirable consequences which would naturally flow from any requirement that the transaction be recast into a series of sales. The Commission found:

> "The present transaction precludes triggering of Transco's gas purchase contracts covering gas produced in Texas which might otherwise occur under a typical gas purchase contract. In addition, the instant arrangement allows the parties considerable operating

[2] The Commission found that Texaco has an adequate gas supply, that its refinery constitutes an adequate market, that it has reasonable and feasible facilities, that it is financially able to perform its contractual undertaking and that the project is economically feasible.

flexibility in that specific leaseholds are not dedicated. The proposed service also will benefit Transco's other jurisdictional customers from a cost standpoint. The record indicates that the jurisdictional transportation revenues will exceed the associated incremental costs by about $600,000 annually.

"None of the foregoing benefits would be available to Transco's jurisdictional customers if the proposed transaction were viewed as a sale from Texaco to Transco and a resale back to Texaco. The latter would be a nonjurisdictional direct industrial sale and hence immune from consideration in a rate proceeding." (J.A. 2037-38)

In contrast, Petitioner has completely failed to suggest what additional factors the Commission should have considered and what additional public interest benefits would have been obtained had the Commission required the Transco-Texaco arrangement to be artificially recast into a series of sales or exchanges.

To reform the transportation agreement into a sale and resale arrangement would be to pervert completely the basic legal relationships contemplated by the parties. It would also conflict with the principles announced in *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965), involving "in place" sales of natural gas where the substance rather than the form of the transaction was held to be controlling. The following factors clearly establish the parties intended a bona fide transportation arrangement and not a subterfuge for a jurisdictional sale:

(1) Texaco is receiving no sales revenue from Transco under the transportation arrangement but

rather is paying Transco to perform a transportation service.[3]

(2) Ownership or title of the gas delivered by Texaco to Transco in Texas and Louisiana does not pass to Transco and such gas does not become part of Transco's gas inventory available for sale to third parties.

(3) The transportation agreement in no way affects Transco's cost of purchased gas as reflected in its resale rates to its distribution customers.

(4) Risk of loss in force majeure situations is shared by Texaco even after delivery to Transco with Texaco remaining completely liable for all present or future gathering, severance or other taxes pertaining to the transport gas whether applicable prior to delivery in the field to Transco or after receipt by Texaco in New Jersey.

(5) The rate paid by Texaco to Transco for the transportation service is directly based upon the transportation component of Transco's contract-demand rate.

The above factors clearly distinguish the subject transportation arrangement from the mutual exchange of gas transactions reflected by the Commission's holdings in *Oklahoma Natural Gas Co.*, 23 F.P.C. 291 (1960), and *Shell Oil Co.*, 25 F.P.C. 1316 (1961), relied upon by Public Service.

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[3] Therefore, it cannot seriously be contended that an attractive unregulated market has been created which permits favored producers to make sales at prices in excess of the Commission's approved rate ceilings. This was the situation which this Court found in *Lo-Vaca* where the transaction admittedly involved a producer sale and the only issue was whether such sale was in interstate commerce and subject to Commission jurisdiction as a result of commingling.

Petitioner's reliance upon *Connecticut Light & Power Co.* v. *F.P.C.*, 324 U.S. 515 (1945), and *F.P.C.* v. *Southern California Edison Co.*, 376 U.S. 205 (1964), is also misplaced. The arrangements at issue in these cases were concededly *sales* in the first instance. The issue was whether such sales were *in interstate commerce* rather than intrastate commerce by virtue of commingling. In *Lo-Vaca* the transaction also involved a producer *sale* with the question presented being whether such sale was *for resale* when the pipeline purchaser in spite of commingling sought to allocate by contract such gas supply to its system compressors. The Commission and the courts have never held that the commingling doctrine was an appropriate basis for converting a transaction which was never intended to be a "sale" into a sales relationship. Therefore, the above cases are clearly inapposite and in no way in conflict with the holdings below. In its initial *Lo-Vaca* decision, the Commission expressly recognized that the "interstate commerce" issue was separate and apart from the question of whether the transaction contained the jurisdictional element of a "sale." *Lo-Vaca Gathering Co.*, 26 F.P.C. 606, 611 (1961). It further stated that it did not intend to apply the commingling doctrine to transportation arrangements such as those present in the instant case (26 F.P.C. at 611).

For the same reason, there is no conflict between the holding of the court below and the Fifth Circuit in *Louisiana Public Service Comm'n* v. *F.P.C.*, 359 F. 2d 525 (1966), *cert. denied*, ... U.S. ..... 17 L ed 2d 68, 87 S. Ct. ..... (1966). That case also involved an acknowledged pipeline *sale for resale* with the only issue being whether the transaction was *in interstate commerce* as a result of deliveries being made from the pipeline's commingled interstate stream.

Over the years the Commission has approved numerous transportation arrangements of a type similar to that au-

thorized here. It presently has on file 25 transportation rate schedules by 13 different pipelines. (J.A. 2035) To accept the argument urged by Public Service would for all practical purposes extinguish the Commission's long standing independent jurisdiction over transportation for hire in the case of every pipeline company which also carries its own wholesale gas for resale. This would have an extremely disruptive effect upon the industry and require material revision of many existing contractual arrangements and substantial additional filings and hearings. In many instances, it would result in the jurisdictional revenues presently received by the pipeline for transportation services becoming non-jurisdictional as a result of the final phase of such transactions becoming recast into direct industrial sales. Not only would substantial new rate design problems be created, but the net effect would be to exempt a great many more revenues from the Commission's jurisdiction than would ever be added by artificially recasting the first phase of traditional transportation arrangements into a sale or exchange.

Petitioner's suggestion that similar transportation arrangements will spread to other refineries or petrochemical companies is unsupported by the record and the experience of the past two years following the Commission's approval of the Transco-Texaco transportation service on February 17, 1965. To the extent future transportation projects may be proposed, they will, of course, be fully subject to Commission review and authorized only where consistent with the public convenience and necessity.

The Commission's recent decision in *Florida Gas Transmission Co.*, Docket No. CP65-393, Opinion No. 516, issued March 1, 1967, is irrelevant to the issues presented in the instant case. That proceeding involved a direct producer field sale to an electric generating company who contracted

with an interstate pipeline company for transportation from the field to the point of consumption. Issues relating to a direct producer field sale combined with a transportation arrangement are not raised in the instant case where there is no producer sale. Therefore, they must await subsequent adjudication. This fact was made clear by the Commission in its opinion below:

> "An essential feature of this transaction is that Texaco is the owner of the gas both at the beginning and the end of its journey from the wellhead to the point of ultimate consumption. It has merely contracted for conventional transportation arrangements subject to the Commission's jurisdiction. *While transfers of gas from a producer to a pipeline or from a pipeline to a direct customer may be treated as a sale for regulatory purposes in appropriate circumstances, we see no reason to do so in the circumstances of this case* where it is clear that the intermediate transactions result in returning the gas to the original producer-owner and no jurisdictional question is involved. In reaching this determination *we do not decide the status of the other types of transactions, such as that presented in the X-20 case.*" (J.A. 2037)[4]

Public Service's contention that Texaco may purchase gas from other producers or royalty owners to utilize in the transportation service is entirely inaccurate and unsupported by the record. It was summarily dismissed by the Commission on rehearing. (33 F.P.C. at 819-20).

The narrow facts of this case wherein a producer has arranged for the transportation of his own gas as an incident to that same producer's ultimate consumption of such gas have not created a broad legal precedent of sweeping impact upon the natural gas industry. The holdings of the court and Commission below are consistent with prior

[4] All emphasis herein supplied.

judicial decisions. Moreover, the legislative history of the Natural Gas Act recognizes transportation as a separate and distinct jurisdictional activity of natural gas pipeline companies. Petitioner's attempt to use this case as a vehicle to obtain advisory rulings covering totally different fact situations presented in other cases or which it speculates may arise in the future is manifestly improper.

B. The Commission Correctly Found That Texaco's Refinery Delivery Line Does Not Require Certification Under the Natural Gas Act

The Texaco produced gas transported by Transco is redelivered to Texaco at a meter station on Transco's transmission line approximately 4½ miles from Texaco's refinery. The lower court and the Commission correctly found that this delivery line was an integral part of Texaco's existing refinery facilities and that interstate commerce ceased when the transported gas was redelivered to Texaco at Transco's meter station. These holdings are consistent with prior Commission precedent and in no way inconsistent with this Court's decision in *F.P.C.* v. *East Ohio Gas Co., et al.*, 338 U.S. 464 (1950) relied upon by Petitioner.[5] In *East Ohio*, the gas was not delivered to the purchaser for own-use consumption but rather for further resale, thereby continuing the chain of interstate commerce. Moreover, the holding in *East Ohio* relied upon by Petitioner was subsequently modified by Congress. The Natural Gas Act was amended March 27, 1954 (68 Stat. 36) to add Section 1(c) which exempts from FPC jurisdiction the

[5] The Commission has consistently held that delivery lines constructed by the customers of interstate pipelines making direct industrial sales are not required to be certificated. *Anchor Hocking Glass Corp.*, 2 F.P.C. 930 (1941); *Jersey Central Power & Light Co.*, 9 F.P.C. 717 (1950); *Montana Power Co.*, 10 F.P.C. 950 (1951); *Reynolds Metals Co.*, letter order of March 27, 1959.

transportation of natural gas received at the boundary of the state if such gas is ultimately consumed within such state.

The contention that the Commission's failure to certificate Texaco's refinery lead-in line creates "a regulatory gap" is not worthy of serious consideration. It is difficult to comprehend exactly what Public Service would have the Commission regulate since no rate will be charged or paid in connection with the operation of this small own-use line and the only party who could be affected by its operation is Texaco itself. Moreover, such line is fully subject to all applicable statutes and regulations of the State of New Jersey and the New Jersey Board of Public Utility Commissioners.[6]

The issues relating to Texaco's own-use delivery line clearly raise no questions of general importance with respect to the Commission's administration of the Natural Gas Act and the holdings of the Commission and lower court are not in conflict with prior precedent.

C. The Transportation Service is in the Public Convenience and Necessity

It has been evident from the outset of this proceeding that due to the basic economics involved, Texaco's Eagle Point Refinery could never be a potential natural gas customer of Public Service. In an attempt to defeat or delay the transportation service, however, Public Service has raised every conceivable objection including: the preemption of available pipeline capacity; the alleged loss of cheap

[6] On September 28, 1964, the New Jersey Board of Public Utility Commissioners certified that Texaco's refinery lead-in line complied with all requirements of the Board's Administrative Order 14:295 under the Natural Gas Safety Act, Title 48 N.J.S.A., Chap. 10.

expansibility; the availability of valley capacity; the need by Texaco and the economic advantage to it of the proposed service; and the alleged lack of public interest benefits. Petitioner's attacks have clearly been "shot gun" in nature and generally relate to matters which would not directly affect Public Service even if its arguments were accepted. These issues were comprehensively dealt with by the Examiner in a lengthy opinion (J.A. 1758-1808) which was adopted by the Commission. The court below correctly noted the limited scope of judicial review under Section 19(b) of the Natural Gas Act and that the Commission's findings are conclusive if supported by "substantial evidence." After examining the record in its entirety, the court accepted the Commission's expert judgment and concluded that the challenged findings of fact were based upon "a thoughtful consideration of the evidence as a whole and a discriminating evaluation of competing factors."

This case does not present an issue of which of two competing alternative sources of gas supply is required by the public interest. Despite urging by the Commission Staff, Public Service completely failed to present during the hearings below a concrete proposal to supply firm and interruptible gas to Texaco's refinery on any basis other than that provided by its filed rates. The purchase of natural gas from Public Service at such rates would increase the present fuel bill of the refinery by over $2,000,000.00 per year. The Commission found that this increased fuel cost would overwhelmingly offset the economic advantage to be derived by utilizing natural gas over fuel oil as a refinery fuel.

Public Service seeks to usurp the benefits flowing from natural gas consumption at the Eagle Point Refinery for its private service area and its stockholders. In contrast, the proposed transportation arrangement provides benefits

inuring to *all* of Transco's customers of (1) a minimum return on the investment in facilities of 12.64%, (2) an improvement in load factor; and (3) an interruptible rate contributing approximately 20¢ per Mcf to the fixed cost of Transco's system. A denial of Transco's certificate application resulting in the continued burning of fuel oil at the Eagle Point Refinery would deprive the customers of Transco and Texaco of these special benefits and offer no offsetting public interest considerations.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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